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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

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FEDERAL COMMUNICATIONS COMMISSION
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In the Matter of)

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)
Rulemaking to Amend Parts 1, 2, 21, and 25)
of the Commission's Rules to Redesignate)
the 27.5-29.5 GHz Frequency Band, to)
Reallocate the 29.5-30.0 GHz Frequency Band,)
to Establish Rules and Policies for Local)
Multipoint Distribution Service and for)
Fixed Satellite Services)

CC Docket. No. 92-297

COMMENTS OF WEBCEL COMMUNICATIONS, INC.

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SUMMARY

This is the second time in a year that the Commission has sought public comment on whether bidding eligibility restrictions should be imposed on incumbent LECs and cable television MSOs for LMDS spectrum. WebCel, a start-up firm dedicated to the commercial deployment of LMDS as a broadband, competitive alternative for local exchange telecommunications, video services, and Internet-related enhanced services, commends the Commission for its explicit recognition that LMDS is capable of delivering a wide array of interactive, broadband communications services. Yet we are very concerned that the Commission's failure promptly to resolve this important question after considering LMDS licensing for four years will unnecessarily delay licensing of LMDS providers and offer an opportunity for the incumbent monopolies to "hamstring" potential entrants through procedural diversions.

Transitional, geographically limited eligibility restrictions barring incumbent LECs and cable system operators from bidding on LMDS spectrum for license areas in which they continue to hold monopoly power are manifestly in the public interest. In these comments, WebCel reviews the evidence already in the record of this proceeding, demonstrating that LMDS eligibility restrictions are needed to prevent incumbent LECs and cable systems from foreclosing the entry of facilities-based competition by using their monopoly rents to purchase and effectively "warehouse" LMDS licenses. We also examine other statutory and Commission rules banning participation by LECs and cable systems in competitive services, concluding that the same analysis and policies should apply to LMDS. WebCel also presents a specially prepared economic report, conducted by Kenneth C. Baseman of MiCRA, which concludes based on well-recognized economic research and literature that "[i]ncumbent monopolists place

an anticompetitive valuation on LMDS licenses” and that bidding eligibility restrictions improve consumer welfare by “provid[ing] social benefits without imposing social costs.”

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COMMENTS OF WEBCEL COMMUNICATIONS, INC.

WebCel Communications, Inc. ("WebCel") by its attorney, hereby submits these comments on eligibility rules and related issues for Local Multipoint Distribution Service ("LMDS") in response to the Fourth Notice of Proposed Rulemaking ("Fourth Notice") in the above-captioned proceeding.¹

INTRODUCTION

This is the second time in one year that the Commission has sought public comment on whether bidding eligibility restrictions should be imposed on incumbent local exchange carriers ("LECs") and cable television multiple system operators ("MSOs") for LMDS spectrum. In its July 1995 *Third Notice of Proposed Rulemaking*,² the Commission inquired whether "[g]iven the

¹ *Rulemaking to Amend Parts 1, 2, 21, and 25 of the Commission's Rules to Redesignate the 27.5-29.5 GHz Frequency Band, to Reallocate the 29.5-30.0 GHz Frequency Band, to Establish Rules and Policies for Local Multipoint Distribution Service and for Fixed Satellite Services*, First Report and Order and Fourth Notice of Proposed Rulemaking, ¶¶ 105-36, CC Docket No. 92-297 (released July 22, 1996)("Fourth Notice").

² *Rulemaking to Amend Parts 1, 2, 21, and 25 of the Commission's Rules to Redesignate the 27.5-29.5 GHz Frequency Band, to Reallocate the 29.5-30.0 GHz Frequency Band, to Establish Rules and Policies for Local* (Footnote continued on next page)

LECs' current monopoly status with regard to the provision of local exchange service . . . [they] would be likely to acquire LMDS spectrum as a means of forestalling competitive entry into the local exchange market, for instance by warehousing spectrum or diverting it to less optimal uses.”³

Unlike the *Third Notice* which also questioned whether LMDS technology could be used to provide telephone service,⁴ the *Fourth Notice* concludes that “LMDS is uniquely positioned to provide competitive telecommunications services and video programming delivery because of its large potential for two-way broadband capabilities.”⁵ Yet despite the lack of record evidence suggesting that LECs or MSOs could offer economies of scope or other efficiencies in LMDS—and in spite of the clear economic and policy basis for auction rules that ban incumbent LECs and cable systems from controlling LMDS licenses where they have monopoly service territories—the Commission has once again asked for comment on a wide variety of economic and policy questions bearing upon the need for and function of cross-ownership restrictions for LMDS.

As a recently incorporated, entrepreneurial venture dedicated to the commercial deployment of LMDS as a broadband, competitive alternative for local exchange telecommunications, video services, and Internet-related enhanced services, WebCel commends the Commission for its explicit recognition that LMDS is capable of delivering a wide array of interactive, broadband communications services. The *Fourth Notice*'s request for specific

Multipoint Distribution Service and for Fixed Satellite Services, Third Notice of Proposed Rulemaking and Supplemental Tentative Decision ¶¶ 97-108, CC Docket No. 92-297 (released July 28, 1995)(“Third Notice”).

³ *Id.* ¶ 101.

⁴ *Id.*

comment on the possible use of LMDS as a means of offering competition for local telephone service and video programming distribution clearly demonstrates that the Commission shares WebCel's vision of the immediate potential for this new service to serve as a significant deconcentrating force in local telecommunications marketplaces that are still subject to both LEC and MSO monopoly power. Particularly in light of the important goal under the Telecommunications Act of 1996 of facilitating the development of effective, facilities-based competition for local telephone services and video programming delivery, WebCel believes that transitional, geographically limited eligibility restrictions barring incumbent LECs and cable system operators from bidding on LMDS spectrum for license areas in which they continue to hold monopoly power are manifestly in the public interest.

WebCel is very concerned, however, that the Commission's reexamination of eligibility restrictions will send the wrong signals to both the capital marketplace and particularly to new, start-up companies like WebCel that are preparing to participate in auctions for this very valuable spectrum resource. The capital markets demand clear, unambiguous policies guarding against the inclusion of monopolists in auctions, because LECs and cable systems have a recognized economic incentive, and the financial resources, to preempt competitive entry by buying up LMDS licenses in their service areas. Like PCS and other spectrum resources the Commission has allocated via auction, LMDS can serve as the means for telecommunications entry by entrepreneurial firms, for whom access to investment capital is crucial.⁶ After four

⁵ *Fourth Notice* ¶ 125.

⁶ Unlike PCS, however, LMDS is unique in its stationary, broadband capability. "LMDS is a complete broadband infrastructure." Thomas Kilgo, Texas Instruments Corp., Presentation at the FCC's "Auctions 1996" Conference, March 15, 1996, Washington, D.C.

years of uncertainty, if the Commission does not resolve the issue of LMDS eligibility quickly, allowing sufficient time for investment capital managers to analyze the FCC's complete rules, identify possible risks, and create auction strategies, the financial resources that are now being positioned for use in LMDS may of necessity be redeployed to other ventures, depriving the Commission—and ultimately the Treasury and the public—of the benefits of their participation as fresh entrants into today's monopoly local telecommunications markets.

Against this background, WebCel addresses a number of issues in its comments. First, WebCel reviews the comments and evidence already in the record of this proceeding, demonstrating that LMDS eligibility restrictions are needed to prevent incumbent LECs and cable systems from foreclosing the entry of facilities-based competition by using their monopoly rents to purchase and effectively “warehouse” LMDS licenses. Second, WebCel examines other statutory and Commission rules banning participation by LECs and cable systems in competitive services, concluding that the same analysis and policies should apply to LMDS. Third, WebCel presents a specially prepared economic report, conducted by Kenneth C. Baseman of MiCRA and attached to the comments as Exhibit A, which concludes based on well-recognized economic research and literature that “[i]ncumbent monopolists place an anticompetitive valuation on LMDS licenses” and that bidding eligibility restrictions improve consumer welfare by “provid[ing] social benefits without imposing social costs.”⁷ Finally, WebCel responds in detail

⁷ *The Economics of Bidding for Scarce Resources: The Lessons of Monopoly Preemption as Applied to FCC Auctions of LMDS Licenses*, Kenneth C. Baseman, MiCRA, August 12, 1996, at 1 (“Baseman Report”) (Attached as Exhibit A).

to the questions in the *Fourth Notice* respecting the potential applications of LMDS service and practical mechanisms for applying eligibility restrictions in the auction context.

In sum, the Commission's decision to seek additional comment on LMDS auction eligibility rules will be a valuable exercise *if* the Commission focuses directly on the key economic and policy questions related to temporary and geographically circumscribed cross-ownership restrictions. As a policy matter, the FCC has adopted, at the express direction of Congress, the objective of stimulating facilities-based competition in local telecommunications,⁸ a goal that fully supports reserving the use of a unique national resource like LMDS to entities who will apply the spectrum to compete with incumbent LECs and cable systems. As an economic matter, the fact is that incumbent LECs and MSOs will find it rational to outbid potential competitors for LMDS because this new resource is among the best, and the clearest short-term vehicle for facilities-based broadband competition. The *Fourth Notice's* stated concerns with respect to potential LEC and MSO efficiencies are off-point, because as the Baseman Report concludes, "there are no plausible efficiencies" arising from joint provision of wireline telephone or cable services and LMDS.⁹ The government therefore has everything to gain, and nothing at all to lose, from a transitional rule barring LECs and MSOs from controlling LMDS spectrum in their service territories while they still enjoy monopoly power over their "core" telephone and video services.

⁸ On August 1, 1996, for instance, the Commission adopted a policy of "maximum flexibility" for CMRS providers, thus for the first time allowing fixed and hybrid fixed-mobile use of cellular and paging licenses, in order to encourage potential competitors to construct competing facilities to those of the wireline local exchange carrier.

⁹ Baseman Report at 5.

DISCUSSION

Since its formation in early 1996—after the close of the comment period in the this docket—WebCel has urged that the Commission develop auction eligibility and “buy-out” regulations for LMDS in order to assure that this revolutionary new wireless service has a fair opportunity to develop as a source of full broadband local telecommunications and cable competition.¹⁰ The *Fourth Notice* asks for comment on a wide variety of technical, economic and policy questions related to whether incumbent LECs and MSOs should be permitted to participate in LMDS auctions for license areas, *i.e.*, BTAs, in which they provide service.

WebCel is pleased that the *Fourth Notice* recognizes both the potentially significant deconcentrating effect of LMDS and the anticompetitive risk arising from unrestricted LEC and MSO participation in this unique new wireless service. Yet WebCel is also concerned that the Commission’s failure to resolve this important question after considering LMDS licensing for four years—and after previously seeking public comment on cross-ownership restrictions in the 1995 *Third Notice*—will unnecessarily delay licensing of LMDS providers and offer an opportunity for the incumbent monopolies to “hamstring” potential entrants through procedural diversions.

There is no serious question that LMDS eligibility restrictions are in the public interest and necessary to prevent the anticompetitive use of this revolutionary new service by incumbent LECs and cable MSOs. The record in this docket provides overwhelming evidence that allowing

¹⁰ See, e.g., *Letter from Glenn B. Manishin, Counsel to WebCel, to Reed E. Hundt, Chairman*, CC Docket No. 92-297, April 16, 1996 (“WebCel Ex Parte”); *Letter from Glenn B. Manishin, Counsel to WebCel, to Reed E. Hundt, Chairman*, CC Docket No. 92-297, June 3, 1996.

these monopolists to bid on LMDS licenses, within their service areas, while they still hold monopoly power will lead to the foreclosure of an important new form of facilities-based competition. This is particularly true in the near term, when LECs will be for the first time be offering unbundled network elements to other firms for competitive local telephone services, and where both LECs and cable systems will not yet face effective facilities-based competition. As the Baseman Report makes clear, *it is a rational business strategy for incumbent monopolists to apply future monopoly rents to outbid potential entrants for scarce alternatives, because such "partial preemption" of competitive entry is "always profitable."*¹¹ Thus, by permitting monopoly LECs and cable systems to purchase LMDS licenses at the very time where the potential for facilities-based local competition is first beginning to emerge, the absence of bidding eligibility restrictions would delay realization of this potential competition for years.

One of the key reasons for this result are the staggering financial resources required for local competition, in both telephony and video programming, via either "wired" networks or mobile wireless services. Simply put, the cost of constructing "fiber to the home" or other sorts of competitive broadband local networks is so huge that building this infrastructure will take years, if not decades.¹² In contrast, LMDS is a cost-effective, efficient and relatively rapid way of delivering alternative and directly competitive broadband voice, data and video services to American consumers; LMDS systems can be up and running well before other significant competition to LECs and cable systems will be available, at any significant scale, from other

¹¹ Baseman Report at 3.

¹² AT&T has estimated that "it would cost \$29 billion to build local facilities to reach 20 percent of consumers in the country's most densely populated areas." *Resale Splits Cable, Long-Distance Firms*, Multichannel News, at 54, July 29, 1996.

forms of facilities-based competition. Consequently, in the short run the economic incentives of incumbent LECs and cable MSOs to preemptively gain control of LMDS spectrum resources in order to foreclose competition are enormous, because LMDS is perhaps the most promising form of facilities-based competition. in the near term, for their “core” monopoly services.

I. THE RECORD CLEARLY DEMONSTRATES THAT LEC AND CABLE SYSTEM ELIGIBILITY RESTRICTIONS ARE NECESSARY TO SPUR FACILITIES-BASED LOCAL COMPETITION AND AVOID ANTICOMPETITIVE ABUSE OF THE AUCTION PROCESS

The *Fourth Notice* cannot be read in isolation, because the Commission’s July 1995 *Third Notice* has already provided ample opportunity for comment on the competitive and consumer welfare benefits or LMDS auction eligibility restrictions. The fact is, however, that none of the LECs or cable systems have yet been able to fashion a credible argument, let alone present any economic evidence, that their participation in LMDS services would spur competition or result in efficiencies (*i.e.*, cost savings) from which consumers would benefit. As the *Fourth Notice* states, the LECs argued only generally that “diversity of services and technology” favors an open entry policy, while most commenters “make the same arguments [favoring] cable eligibility that they made for LEC eligibility.”¹³

The beneficiaries of unrestricted LMDS eligibility thus have nothing to point to, except for rhetorical concerns about open entry, in support of allowing LECs and MSOs to control LMDS services notwithstanding their monopoly status. Perhaps more importantly, the record in this proceeding is uncontradicted that eligibility restrictions are necessary to spur facilities-based

¹³ *Fourth Notice*, ¶¶ 112-13.

local competition and avoid anticompetitive abuses of the auction process. WebCel's April 16, 1996 *ex parte* comments, which produced a flurry of activity on this issue in the Spring of 1996, noted that:

[T]he Commission's Order in the LMDS proceeding . . . must include necessary safeguards to avoid outright takeover of another potential competitor and anticompetitive abuses by the [LECs] and [MSOs]. These entities have substantial economic incentives to forestall deployment of LMDS as a direct substitute for their facilities-based, monopoly networks.

* * * * *

Simply put, WebCel believes that *LMDS is the best short-run form of effective facilities-based competition with incumbent, monopoly LECs and cable MSOs*. The development of such competing local networks—in order to release the current monopoly bottlenecks held by the LECs and MSOs, for the benefit of all consumers—is a central goal of the landmark Telecommunications Act of 1996.

* * * * *

Implementing the Act's charter for facilities-based local competition requires that the Commission take strong action to prevent monopoly carriers from using their dominant economic power to stifle competitive entry. In an auction environment this is doubly important, because the Commission only has one chance to set the right "rules of the road" for real competition. Where a revolutionary service like LMDS is involved, it is imperative that the Commission get it right the first time.

WebCel Ex Parte at 1-2 (emphasis in original).

The economic problem at the heart of WebCel's proposal for eligibility restrictions on LEC and cable operator participation in LMDS "in region" is that as monopoly incumbents, these firms are specially positioned to foreclose use of this spectrum as a form of potential competition for their own services. "LECs and MSOs will have an inherent advantage when bidding against [new entrants], because it is economically rational for them to bid 'above-market' prices for spectrum where the potential loss in monopoly profits to them exceeds the stand-alone present value of the spectrum to an unaffiliated entity." *Id.* at 5. Thus, the inclusion

of these incumbents in auctions for spectrum that holds the clear, short-run potential for reducing their market power (and monopoly profits) would easily result in the failure of LMDS technology to be exploited fully, rather consigned to use as an adjunct, “complementary” service that does not threaten the vastly larger core LEC and cable operator revenue streams and monopoly profits.

These straightforward propositions are supported by a wide array of parties—from consumer advocates, to state competition enforcers, to local telecommunications entrants—all of whom echoed WebCel’s concern that without transitional bidding restrictions precluding LECs and MSOs from participating in the LMDS auctions, the incumbent monopolists would have a powerful economic incentive to acquire LMDS spectrum largely in order to prevent its application as a form of direct facilities-based competition for their existing monopoly services and customers.

- The Consumer Federation of America commented eloquently that “[w]hile nobody can be certain of all the potential applications for LMDS technology, early indications are that it may provide an alternative means for providing the ‘last mile’ to the home. . . . If LMDS can provide broadband video and local telephony competition, it is important that incumbent providers not be permitted to capture this spectrum and thus thwart the development of competitive alternatives.”¹⁴
- The attorneys general of 12 states commented that “it is critical that the Commission develop rules that will preclude the local telephone and cable monopolists from bidding for new LMDS franchises in their regions until there is real competition in their respective local service markets. . . . Without the[se] safeguards, however, it is equally clear that an excellent available alternative for offering a facilities-based direct competitor to the existing local

¹⁴ Letter from Bradley Stillman, Telecommunications Policy Director, Consumer Federation of America, to Reed E. Hundt, FCC, July 3 1996, at 2.

telephone and cable monopolists in the immediate future will, in all likelihood, be lost.”¹⁵

- MCI agreed that because LMDS “may provide the best near-term opportunity for a new facilities-based entrant to offer a wide range of broadband local services in direct competition with the incumbent local exchange carriers and cable television multiple system operators,” the Commission should adopt service, eligibility, and auction rules for LMDS, that “bar LECs and MSOs from bidding on LMDS spectrum, or holding an attributable interest in an LMDS bidder, in any license area (e.g., Basic Trading Area) which overlaps any of their local telephone service or cable franchise areas.”¹⁶

Thus, the existing record before the Commission demonstrates conclusively that eligibility restrictions on LEC and cable system operator participation in LMDS are necessary to bring the benefits of facilities-based local competition to American telephone and video consumers. The Commission has a unique and historic opportunity in this proceeding to craft rules to propel the United States into an era of real local telephone and video competition via LMDS. It can only do so, however, if necessary incentives are created for new entrants *and* safeguards are formulated to protect against anticompetitive use of the auction process itself. Barring LECs and MSOs from bidding for LMDS blocks within their monopoly service regions—until there is effective, facilities-based local competition—is necessary for LMDS to develop as a broadband, competitive local service alternative, and to avoid repetition of the costly mistakes made by the Commission in licensing of other potentially competitive technologies, such as cellular mobile radio.¹⁷

¹⁵ Letter from Thomas W. Corbett, Jr., James E Doyle and Hubert H. Humphrey III to Reed E. Hundt, May 10, 1986, at 2-3. These state officials, subsequently joined by 12 additional attorneys general, *see Fourth Notice* ¶ 124 n.211, agree with WebCel that the Commission has a unique and time-limited opportunity to fashion bidding and license eligibility rules that prevent incumbent LECs and MSOs from using their monopoly profits to “lock up” LMDS and snuff out a new form of facilities-based local competition.

¹⁶ Letter from Donald F. Evans, Vice-President, MCI, to Reed E. Hundt, FCC, May 24, 1996 at 2.

¹⁷ *See, e.g.,* WebCel Ex Parte at 7.

II. LMDS ELIGIBILITY RESTRICTIONS ARE FULLY CONSISTENT WITH OTHER STATUTORY AND COMMISSION RULES BANNING PARTICIPATION BY LECs AND CABLE SYSTEMS IN COMPETITIVE SERVICES

The *Fourth Notice* indicates that the 1996 Act “contains a number of provisions designed to facilitate the entry of LECs and cable operators into each others’ markets.”¹⁸ While it is true that the Act indeed contemplates competition between telephone and cable companies, for instance by its repeal of the Commission’s telco-cable cross-ownership ban, there is nothing to suggest Congress wanted either to overrule all licensing eligibility restrictions on incumbent monopolists or to encourage LECs and cable operators to compete with each other principally using stand-alone, wireless spectrum resources (while avoiding their previous commitments to upgrade their monopoly networks).

The most significant indication of the policies underlying the 1996 Act are in the “anti buy-out” provisions related to telephone entry into cable television services. Section 652 of the Act provides that no LEC can buy more than a 10 percent interest in a cable system in its franchise area, or vice-versa, unless the cable system operates in a competitive, multi-provider marketplace and is not affiliated with a major MSO.¹⁹ The intent of these provisions is clearly to maximize competition between cable and telephone providers by forcing them to “build, not buy”—in other words, as the House Report on the 1996 Act stated, to make good on their repeated promises to “modernize their communications infrastructure.”²⁰ They also make clear that Congress *does not want either incumbent LECs or cable systems to gain immediate control*

¹⁸ *Fourth Notice* ¶ 119.

¹⁹ 47 U.S.C. §§ 652(a), (b), (d)(3).

over new, direct competitors, at least until core monopoly services are subject to effective local competition.

In the same way, the transitional LMDS eligibility restrictions proposed by WebCel would share these policies.²¹ First, limited restrictions would incent LECs and cable systems to upgrade their networks to two-way broadband functionality, thus promoting competition in a way that maximizes efficiency by encouraging joint use of common plant for multiple video and telephone services. Second, the limits would remain in place only until the “core” monopoly markets became subject to effective competition, precluding incumbent LECs and cable systems from bidding for or acquiring LMDS licensees—direct competitors—while they retain market power.

These are also the same considerations justifying a pair of current cross-ownership restrictions in analogous markets, one (for MMDS) modified by the 1996 Act, the other (for PCS) reaffirmed by the FCC after passage of the Act. With respect to MMDS, a wireless technology particularly well-suited to delivery of broadcast video (and frequently referred to as “wireless cable”), Section 202(I) of the 1996 Act amended, and retained, the cable-MMDS cross-ownership ban to provide that cable operators are precluded from holding MMDS licenses within their franchise areas until the cable system “is subject to effective competition.”²² Similarly, just recently the Commission modified its cellular-PCS cross-ownership rules, yet reaffirmed that a special restriction on cellular licensees—for whom PCS will likewise represent a form of direct

²⁰ H. Rep. No. 104-204, 104th Cong., 1st Sess. 53 (1995).

²¹ See WebCel Ex Parte at 2.

²² 47 U.S.C. § 533(a)(2)

facilities-based competition—is appropriate. The Commission concluded that an eligibility restriction is justified because:

Economic theory teaches that auctions are won by the bidder who puts the highest value on the property being auctioned. The value of the PCS licenses to the incumbent providers would be their continued economic rents (profits in excess of economic costs), which could be higher than the anticipated profits of new entrants into a more competitive market. Incumbent firms may thus be willing to pay even more for the chance to impede entry than for the chance to compete vigorously against new entrants.²³

These same considerations, again, support WebCel's proposal for transitional auction eligibility rules that would bar LECs and cable systems from bidding for or controlling LMDS licenses in their services area until effective, facilities-based competition develops for their monopoly services. It is limited in time, like the revised cable-MMDS restriction, to the period in which the incumbent retains monopoly power, and hence eliminates the monopolist's incentive to forestall facilities-based local competition. It is also targeted to those parties, like the cellular-PCS rule, exclusively within their service territories, where they would have an anticompetitive incentive to wield their "continued economic rents" in an effort to subvert fair competition in the auction process.

The *Fourth Notice* repeats a tentative finding from earlier in this proceeding that existing statutory and regulatory restrictions do not specifically address LEC and cable system acquisition of LMDS licenses.²⁴ To the extent, if any, that the Commission may be suggesting it lacks the authority to fashion rules specifically applicable to a new service LMDS, that is clearly not the

²³ *Amendment of Parts 20 and 24 of the Commission's Rules -- Broadband PCS Competitive Bidding and the Commercial Mobile Radio Service Spectrum Cap*, WT Docket No. 96-59, FCC 96-278, ¶ 99 (released June 24, 1996) ("Cellular-PCS Order").

²⁴ *Fourth Notice* ¶¶ 111, 113.

case. To the contrary, the proposed bidding eligibility restrictions for new services are consistent with the 1996 Act and the Commission's post-Act treatment of "non-statutory" cross-ownership restrictions, like cellular-PCS, and would directly further the same policies supporting the Act's cross-ownership and buy-out provisions. As CFA has commented:

The key to success of the Telecommunications Act of 1996 is the development of competition in all sectors of the communications industry. Despite efforts at both the state and federal levels, both the cable and local telephone markets continue to be monopolies. It would be a major blow to competition if the incumbent cable or local telephone operator were permitted to bid on this spectrum and snuff out an important potential competitor before it even has a chance to prove itself in the marketplace.²⁵

III. THERE ARE CONCLUSIVE ECONOMIC REASONS TO BAR LECs AND CABLE OPERATORS FROM BIDDING ON "IN-REGION" LMDS

WebCel's position on the economic bases for LMDS bidding eligibility exclusions has been clear since we first raised the issue with the Commission in April of this year. So long as incumbent LEC and cable system monopolists do not face effective local competition, they have a strong economic incentive to outbid rivals for LMDS spectrum. "The Commission would be fooling itself to believe that an auction is fair or 'efficient' if it includes monopoly carriers, because doing so would only allow incumbent bidders—but not others—to value their auction projections based on the 'opportunity costs' of lost monopoly profits and market share."²⁶

The *Fourth Notice* asks for comment on whether there is an economic incentive for an incumbent to bid successfully at auction and either not use ("warehouse") the spectrum or "divert

²⁵ CFA Ex Parte at 2.

²⁶ WebCel Ex Parte at 6.

it to less competitive uses.”²⁷ It is difficult to see why the Commission felt compelled to reexamine this question, as it reiterated these precise findings just weeks ago in the *Cellular-PCS Order*. Nonetheless, WebCel has asked Kenneth C. Baseman of MiCRA, a recognized expert in telecommunications economics, to review these issues. The Baseman Report (Exhibit A) demonstrates that settled economic doctrine completely supports WebCel’s proposals in this proceeding, because *incumbent monopolists will always find it profitable to “preempt” spectrum resources necessary for direct competition where, as in LMDS, the potentially competitive technology is among the best alternatives for competitive entry, in the near term, with the incumbent’s monopoly services.*

The Baseman Report’s conclusions can be summarized in several key points:

- Monopolists have strong incentives to preemptively gain control of limited scarce resources necessary for competition. Incumbent LECs and cable systems place an anticompetitive valuation on LMDS licenses because control of the licenses means that competition for the monopoly will either be completely or partially foreclosed.
- Preemption of LMDS service by outbidding auction rivals is always profitable and rational economically for monopolist LECs and cable systems because LMDS is one of a limited number of alternatives for facilities-based alternatives for local competition.
- There are no plausible economies of scope or other efficiencies between wireline telephone services and LMDS or between cable service and LMDS. Social costs would only arise from a bidding eligibility restriction if the optimal use of LMDS is as a complement to (rather than a substitute for) existing in-region LEC and MSO services, and if regulations requiring interconnection and nondiscriminatory treatment of competitors are ineffective.
- Use of LMDS as a vehicle for telephone-cable competition is unlikely, because both LECs and cable systems would be in a position to hold credible “hostages”

²⁷ *Fourth Notice* ¶ 130.

that would deter entry by the other and likely lead to a “no entry” stalemate, with each monopolist rationally deciding that the risk to its existing revenue stream outweighs the potential gain from entering the other monopoly.

- Exclusion of LECs and MSOs from “in-region” LMDS auctions will not necessarily reduce the government’s net auction revenues, because an incumbent monopolist need bid only slightly more than the competitive value, and because the presence of monopoly bidders will tend to deter many competitive firms from undertaking the costs and risks of preparing for and participating in the auctions. Adding LECs and MSOs as bidders will not increase the number of bidders, and hence potential revenues, if other bidders drop out.

These economic considerations will be discussed in more detail in Section IV of these comments, in which WebCel responds to the Commission’s specific questions on LMDS eligibility. Suffice it to say, however, that we believe the record supports only one conclusion. LMDS eligibility restrictions are needed to protect consumer welfare and to facilitate local telephone and video delivery competition. Use of this unique resource by either LECs or MSOs to offer “complementary” services (*e.g.*, video-on-demand for MSOs or teleconferencing for LECs) would deprive consumers of an important source of facilities-based local competition for both telephone and cable services. Use of LMDS by either telephone or cable systems to compete for the “other” service would be equally inconsistent with the public interest, because if the choice is between two competitors or more in the battle to offer broadband services to consumers, regulators should choose methods to maximize the number of competitors. The only way to fashion a real market test for local telephone and cable competition is to ensure that competition is not limited to the two current monopolists.

IV. THE COMMISSION SHOULD IMPOSE TRANSITIONAL, GEOGRAPHICALLY LIMITED LMDS ELIGIBILITY RESTRICTIONS, DRAWING ATTRIBUTION AND RELATED IMPLEMENTATION RULES FROM ITS ANALOGOUS RULEMAKINGS

The *Fourth Notice* concludes that “the record of this proceeding strongly supports the conclusion that LMDS will provide a unique and important source of competition to incumbent cable and telephone companies.”²⁸ WebCel strongly concurs with this conclusion, and with the Commission’s similar observation that LMDS is “uniquely positioned to provide competitive telecommunications services and video programming delivery because of its large potential for two-way broadband capabilities.”²⁹ As we have commented previously, at 1,000 MHz (that is, excluding the additional 300 MHz proposed for allocation to LMDS in the *Fourth Notice*), LMDS offers 33 times the bandwidth available for any potential PCS licensee, and can support—within *each* cell—more than 250 digital video channels, well over 18,000 simultaneous voice-grade telephone circuits, or more than 500 interactive data channels operating at about two Mbps capacity, as well as combinations of all of these.³⁰

The *Fourth Notice* also asks for comment on a wide variety of technical, economic and policy questions related to whether incumbent LECs and MSOs should be permitted to participate in LMDS auctions for license areas, *i.e.*, BTAs, in which they provide service. In this section, WebCel responds to the Commission’s questions, with the caveat that we believe repetitive reexamination of these issues is both unwarranted and counterproductive. The Commission has already provided incumbent LECs and cable systems with the opportunity to

²⁸ *Fourth Notice* ¶ 125.

²⁹ *Id.*

³⁰ WebCel Ex Parte at 3.

provide economic and policy support for their entry into LMDS. They failed to do so. The 1996 Act strongly reinforces the conclusion that where facilities-based local competition is concerned, the Commission should structure its rules to stimulate the deployment of competing local networks, a policy the Commission has applied to its recent restructuring of cellular and paging regulations to facilitate fixed and “hybrid” applications. Any new claims for LEC or cable system “efficiencies” in LMDS must therefore be regarded with suspicion, and bear a weighty burden of demonstrating that they outweigh the potential for anticompetitive use of this valuable spectrum resource.

A. Auction Policies. The *Fourth Notice* observes that the Commission avoids “distorting decisions based on sound business judgment,” seeking comment on how to balance “the potential for competition presented by open entry against the possibility that this spectrum may be used to forestall rather than promote competition.” *Fourth Notice* ¶ 125. WebCel agrees that the Commission should not impose regulations without a solid policy justification and an awareness of their economic consequences. We do not believe, however, that this requires the Commission to allow LEC and MSO participation in LMDS merely because of a hypothetical supposition that an eligibility ban might eliminate “new services not now offered by any firm.”³¹

Incumbent LECs and MSOs have monopoly power, and thus have a clear economic incentive to delay or exclude entry and competition. “Incumbent monopolists have incentives to outbid potential entrants for any scarce resources necessary to enter and compete.”³² Just as the 1996 Act’s interconnection provisions for incumbent LECs are designed to use regulation as a

³¹ *Fourth Notice* ¶ 125.

³² Baseman Report at 1.

means of checking market power and eliminating barriers to competition, so too would eligibility limitations be a means of preventing abuse of incumbent monopoly power until meaningful competition develops. *See* WebCel Ex Parte at 1.

B. LMDS Service Capabilities. LMDS in fact is a “unique and necessary resource for de-concentrating the market power of incumbent LECs and cable operators.” *Fourth Notice*

¶ 126. As noted above, LMDS simultaneously can support broadband provision of telephone service, video programming and data services such as Internet access.³³ As Chairman Hundt has observed, LMDS “will deliver hundreds of digital video channels together with telephone and data services.”³⁴

LMDS is different in very significant ways from other wireless services. Its broadband capabilities make LMDS far more robust and less expensive than terrestrial “mobile” wireless services such as cellular and PCS, which require much larger capital investment to support “hand off” and roaming, and far more “local” than satellite-delivered services, which must be configured to cover a far larger geographic “footprint.” LMDS is a highly flexible service, because the spectrum used can be divided quickly and easily among different services (for instance, switched telephony and video) thus making it very responsive to customer demand.

LMDS is technically superior to the spectrum-based services that will be auctioned later, such as 40 GHz, because, as CellularVision has previously shown, there are significant signal

³³ *See* “Independence Day of the Telecom Industry,” Remarks of FCC Commissioner Rachelle B. Chong at Telestrategies Wireless Broadband Conference, Washington, D.C., July 16, 1996, at 3 (“I’m excited about the LMDS vision of offering its customers a rich package of services, things like telephone service, broadcast and interactive video, video teleconferencing, high-speed, two-way data transmission and Internet access. It’s going to be an attractive offering, no doubt about it.”)

propagation differences, and resulting increased technology expenses, associated with other, higher-frequency wireless spectrum blocks. *Fourth Notice* ¶ 29.

C. Efficiencies or Potential Incumbent “Advantages.” The *Fourth Notice* asks for comment on whether there are any “inherent” cost advantages of efficiencies possessed by incumbent LECs or MSOs in providing “in-region” LMDS. *Id.* ¶ 127. There are no such efficiencies or “advantages.”

None of the LEC or cable commenters in this proceeding, as the *Fourth Notice* observes (*id.* ¶ 112-13), have raised any efficiency arguments against an eligibility restriction, let alone proven that there are economies of scope between “wired” telephone or cable services and LMDS. In fact, because LMDS is a wireless service that will not share infrastructure with existing LEC and MSO networks, there is no economic basis for the achievement of any appreciable efficiencies or economies of scope from the joint provision of wired telephony or video services and LMDS. As the Baseman Report concludes, “[t]here are no plausible efficiencies from MSO or LEC control of LMDS spectrum.”³⁵

The *Fourth Notice* also asks whether the “size, experience and financial status” of RBOCs or MSOs would make them “uniquely positioned to be strong LMDS providers.” *Id.* ¶ 128. This is simply not the case. As the Baseman Report notes, neither marketing nor brand names are “at all unique to the LECs.”³⁶ Moreover, capital is highly efficient and available, incumbents have no more experience with either LMDS or broadband wireless services in

³⁴ Wireless Week, June 17, 1996 (quoting Chairman Hundt). Assuming an average urban density, an all-digital LMDS transmitter can deliver data and telecom lines to serve 15,000-18,000 customers while supporting 224 digital video channels across 1 GHz of spectrum, *Id.* (quoting Thomas Kilge of Texas Instruments).

³⁵ Baseman Report at 5.

general than other potential providers, and the size of a potential entrant is irrelevant to the success of their entry. For instance, RBOCs have been claiming since 1984 that repeal of the MFJ's information services ban would allow them to compete vigorously in the enhanced services marketplace, but despite the elimination of that prohibition by the courts in 1990, RBOCs have yet to successfully launch any significant on-line or other information services.

Finally, LECs and cable operators have also been professing the imminent deployment of complementary technologies (such as ADSL and cable modems/telephony, respectively) that will permit them to use their networks to compete with each other immediately. As a policy matter, WebCel strongly believes that the Commission should force these incumbents to make good on their promises—which provided a major reason for congressional elimination of the telco-cable cross-ownership provision—before allowing them to buy up wireless spectrum for those purposes. If the choice is between a duopoly (LEC v. cable) market structure, or a more vibrant, multi-competitor marketplace, policy demands that the FCC choose the latter.

D. Warehousing Incentives. The Fourth Notice inquires whether LECs and MSOs would have an economic incentive to acquire LMDS spectrum “to supplement their existing services rather than face immediate competition.” *Id.* ¶ 129. As WebCel advised the Commission previously, it is clear that incumbents would have just such an anticompetitive incentive, because they value the spectrum more highly than others because of the “opportunity costs” of lost monopoly profits and market share. Any “supplemental” markets (and potential

³⁶ Baseman Report at 5.